

**Honolulu Authority for Rapid Transportation  
City and County of Honolulu**

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL  
REPORTING AND ON COMPLIANCE AND OTHER MATTERS

**Fiscal Year Ended June 30, 2021**



**N&K CPAs, Inc.**

ACCOUNTANTS|CONSULTANTS

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**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER  
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS  
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN  
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Directors  
Honolulu Authority for Rapid Transportation  
City and County of Honolulu

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the Honolulu Authority for Rapid Transportation ("HART"), a component unit of the City and County of Honolulu ("City") as of and for the fiscal year ended June 30, 2021, and the related notes to the financial statements, which collectively comprise the HART's basic financial statements, and have issued our report thereon dated November 30, 2021.

**Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered HART's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the HART's internal control. Accordingly, we do not express an opinion on the effectiveness of the HART's internal control.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify a certain deficiency in internal control, described in the accompanying schedule of findings as item 2021-001 that we consider to be a material weakness.

### **Report on Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the HART's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

### **HART's Response to Findings**

HART's response to the findings identified in our audit is described in the accompanying response of affected agency. However, we disagree with HART's comments that the five misstatements identified by us were not material to HART's financial statements as of and for the fiscal year ended June 30, 2021 and HART's interpretation of a material weakness in internal control over financial reporting. HART's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

### **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*N + K CPAs, INC.*

Honolulu, Hawai'i  
November 30, 2021

## SCHEDULE OF FINDINGS

**Ref.  
No.**

### **2021-001 Financial Statement Reporting**

**Criteria:**

Management is responsible for establishing and maintaining internal control over financial reporting to permit the preparation of the HART's financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP). These accounting principles require financial statements to be prepared using the economic resources measurement focus and accrual basis of accounting. Effective internal control supports timely and accurate financial reporting.

**Condition:**

HART reports on a cash basis throughout the fiscal year and only prepares accrual basis financial statements for its annual report as of and for the fiscal year ended June 30. Accordingly, in preparing accrual basis financial statements, there should be written procedures to clearly define the reporting and closing procedures, the timing of such procedures and the review and approval process involved. Included in the reporting and closing procedures should be account reconciliations that must be prepared, and adjustments that must be recorded in order to properly present timely accrual basis financial statements. This process ensures the accuracy and validity of financial information provided.

During our audit, we identified 5 misstatements that in our opinion, were material to HART's financial statements as of and for the fiscal year ended June 30, 2021. These misstatements were identified by audit procedures performed during the course of the audit, and are indicators that HART's internal controls over financial reporting were either not properly designed or were not operating as designed. The following audit adjustments to correct the financial statements have been recorded by management:

1. An adjustment to decrease intergovernmental revenue and receivable by \$5,517,349 related to the Highway Improvement HDOT agreement for grant funds, since it did not meet the criteria for accrual as of June 30, 2021.
2. An adjustment to decrease other revenue and land additions by \$4,260,528 to correct cancelled checks recorded as revenue and land additions.
3. An adjustment to decrease current assets by \$7,840,112 due to prepaid items with a 5 year amortization period.
4. An adjustment to decrease current liabilities and increase advance from city, noncurrent portion by \$275,000,000 related to advance of Tax-Exempt Commercial Paper funds which were repaid subsequent to year end from G. O. bond series 2021 E funds.
5. An adjustment of \$247,750,677 to the presentation of intergovernmental revenues on the statement of cash flows from cash flows from noncapital financing activities to cash flows from capital and related financing activities.

**Ref.  
No.**

**2021-001 Financial Statement Reporting (Continued)**

**Cause:**

We noted that the accuracy and delay of the preparation of the accrual basis financial statements and the trial balance were affected by the following:

- (1) Account reconciliations not being performed timely;
- (2) Numerous audit and client adjustments proposed after receipt of the initial trial balance;
- (3) Follow-ups with management regarding classification of the information contained in the supporting schedules;
- (4) Insufficient or appropriate resources devoted to timely closing process;
- (5) Inappropriate application of GAAP.

**Effect:**

The preceding issues resulted in delays in receiving the trial balance and an accrual basis financial statements that captured all valid journal entries and accruals, which in turn delayed the audit process.

**Identification of a Repeat Finding:**

This is a repeat finding from the previous audit finding item 2020-001.

**Recommendation:**

We recommend management re-evaluate its annual closing process to clearly define financial reporting and closing procedures, the timing of such reporting and the review and approval process involved. These written procedures should also document the process to ensure the trial balance and financial statement preparation process captures all valid journal entries and accruals, and that the year-end trial balance is complete and accurate.

Management should also consider performing adjustments, including cash to accrual or capitalization of costs, etc., prior to fiscal year end closing, either on a quarterly or semi-annual basis, or at the end of third quarter of the fiscal year. An evaluation should be made by management to determine if additional sufficient and appropriate resources are needed to perform these procedures.

Last, management should properly apply GAAP. The purpose of GAAP standards is to help ensure that the financial information provided to investors, regulators and stakeholders is accurate, reliable, and consistent with one another. Therefore, the improper application of GAAP may lead to incorrect recording and reporting of accounting information, as well as the possibility of producing financial statements that are not complete, consistent and comparable.

**RESPONSE OF AFFECTED AGENCY**



Lori M. K. Kahikina, P.E.  
*Interim Executive Director and CEO*

Rick Keene  
*Deputy Executive Director and COO*

**BOARD OF DIRECTORS**

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Dean Uchida  
Hoyt H. Zia

## HART Management Response to Report on Internal Control over Financial Reporting

### Finding 2021-001 – Financial Statement Reporting

**Management Response:** Management would like to thank the external audit team for the work performed on the current year audit and the recommendation on potential improvements to the financial reporting process. We are committed to ongoing improvements in the Finance Department, particularly regarding internal controls and the accounting and financial reporting processes. We are very pleased that the audit for the year ended June 30, 2021 was completed approximately two months earlier than in the prior year, which is indicative of improvements made in our processes.

As recommended by the auditors, Management commits to continue to evaluate and implement improvements in the accounting and financial reporting processes, including appropriate documentation of the financial reporting and closing procedures and the review and approval process.

While we appreciate the input and recommendation from the external auditors, and with due respect, we disagree that this situation represents a material weakness.

A “material weakness” is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of our financial statements will not be prevented, or detected and corrected, on a timely basis.

With regard to the financial reporting processes for the recently completed audit, it is our opinion that no material misstatement occurred. In addition, several mitigating internal controls are in place that would prevent a material misstatement in the financial statements to go undetected. The auditor’s report notes five adjustments that were made. However, we believe that the net effects of these adjustments were not material to the overall financial statements. We are not necessarily disagreeing with the adjustments being made, but rather the materiality of the adjustments and the conclusion that the situation poses a material weakness to the financial reporting process. We would like to meet with the auditors to further discuss the basis for their opinion on materiality.

The net impact of these five adjustments was:

- A \$9.8 million reduction in non-operating revenues and expenses. This is less than a 4% change.
- A \$13.5 million reduction in current assets, a \$3.6 million increase in non-current assets and a \$9.8 million decrease in total assets, or changes of 7.6%, 0.07% and 0.19%, respectively.
- A reduction of \$275 million in current liabilities and an increase of the same amount in non-current liabilities related to a transaction that occurred subsequent to the end of the period under audit. This transaction was fully described in the footnotes to the financial statements. This adjustment had no net impact on total liabilities.
- A \$247.7 million reclassification between categories of the cash flow statement. For purposes of consistency and comparability, HART presented “Intergovernmental Revenues” in the same category on the Statements of Cash Flows as it had been presented since the beginning of the Project. During this audit, the auditors reclassified this line item for both fiscal years 2021 and 2020. This reclassification resulted in no overall impact to the reported cash position.

We believe the impacts noted above do not represent material misstatements to the overall financial statements.

Given the nature of the HART project, preparing and monitoring cash basis financial results are very important to the management and oversight of the project. We will consider your recommendation of preparing periodic accruals. But whether or not interim accruals are prepared, the year-end accrual process would not significantly change due to the nature of the project and the related timing of the receipt of funding and invoices from contractors. We also want to note that account reconciliations are prepared and adjustments are recorded to present these accrual basis financial statements.

In summary, we appreciate the work of the auditors and their input and recommendation. We respectfully disagree with the categorization of this recommendation as a material weakness. We are very pleased to have improved the completion date of the audit by approximately two months from last year. This was the first financial audit in the past four years that was completed and submitted to the City’s Department of Budget and Fiscal Services on a timely basis. We will consider ways to efficiently prepare accruals on an interim basis. And we commit to further evaluate and continue to improve our financial reporting, closing and review and approval processes.